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LEGAL ISSUES



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Cases of Note — Stealing That Dream Home Design

Copyright — Actual Damages & Disgorgement of Profits

by **Bruce Strauch** (The Citadel) <strauchb@citadel.edu>

Christopher Phelps & Associates v. Wayne Galloway v. Simonini Builders, Inc., United States Court of Appeals for the Fourth Circuit, 2007 U.S. App. LEXIS 3117 (2007).

Wayne Galloway set out to build his retirement home on Lake Wylie, NC south of Charlotte. Given common misconceptions folks have about copyright, the facts are utterly believable. **Galloway** was mad at his architect and went with his son to the more upscale Lake Norman on the other side of Charlotte where he saw the French-country house of his dreams. He asked the builder — **Simonini Builders** — for a copy of the plans. They referred him to the homeowner, **Mrs. Gina Bridgeford**.

She figured she had paid so much for the plans that she owned them. Her only concern was he not put up an identical house near her. **Galloway** told her he was going 30 miles away.

Each page of the plans had a copyright notice of **Phelps & Assoc.** and plainly stating that the purchaser “is authorized to construct one and only one home using this plan. Modification or reuse is prohibited.”

Galloway changed the name and address from **Bridgeford** to **Galloway**, copied the plans and set to work on his home as his own general contractor. Some of the subs phoned **Phelps** asking questions about the windows, and thus **Phelps** got wind of the piracy. One of the subs realized what was going on and tried to warn **Galloway** who replied:

“They’ve got to find me, catch me first.”

Yes, how often you’ve found comfort in that notion when you were blithely photocopying something you shouldn’t. Pages of paper can be cached, but a house does kind of stand out.

Well, **Phelps** did find out and sent **Galloway** a threatening lawyer letter. **Galloway** stopped construction.

Phelps rushed to register their copyright, but you’re up to date on this and know it’s not essential to have copyright, but is essential if you want to sue. Then **Phelps** sued asking for damages, disgorgement of profits and an injunction.

Enjoining what, you ask. And you shall find out directly.

The district court jury gave **Phelps** \$20,000, the fee normally charged for such a design. There were no profits to disgorge.

An injunction used to belong to that old friend the King’s Chancellor; later the Chancery Courts of England and the Equity Courts of the US of A. Which is to say it’s not a jury issue.

The district court denied an injunction, saying **Phelps** had been made whole. **Phelps** wanted the injunction to prohibit the lease or sale of the house and the return or shredding of the plans. **Phelps** of course appealed, or we wouldn’t be reading this.

Interesting. And of course you’ve jumped ahead of me and are asking what will happen when Galloway kicks the bucket. Will his heirs be enjoined from leasing or selling?

We’re in the Fourth Circuit. Appeal goes from NC to Richmond, VA., a courtroom of dire memory where I was once treated with contumely by a three judge panel for trying to create an implied cause of action. But that’s a tale I can tell in the Old Lawyer’s Home.

The Fourth Circuit said the injunction denial was perfectly proper. Giving **Phelps** what they asked for would unduly restrain the alienation of real property.

And of course you’ve already thought of the what if the heirs don’t have the money to pay the taxes. They have to lose the house to the county rather than sell it? And what if there are multiple heirs and they can’t agree on the use of house? The parade of “what ifs” that would force a sale just goes on and on.

The disgorgement of profit **Phelps** sought was measured as the difference between the cost of construction and the value of the house. The architects claimed the house was worth \$1.1 mil for a profit of \$200,000. **Galloway** in turn said he had no profit were it sold, but rather a loss of \$160,000.

The Rest of the Appeal

The trial judge had instructed the jury that the **Bridgeford** house plans were a derivative work which is to say an earlier design had been given a bit of tweaking. And he went on to say **Phelps** only owned the tweaked bits and not the

preexisting material. He seemed to base this on the fact that registration had only been done for the **Bridgeford** plans and not the earlier one it was derived from.

The Fourth Circuit said, yes, that’s true if the underlying work was in the public domain or owned by somebody else. But **Phelps** had done the first drawing that was tweaked into the **Bridgeford** one.

As to the registration of copyright, the filing only serves to provide evidence of copyright and is required before you can file a lawsuit. Copyright attaches when the work is fixed in a tangible medium. See 17 U.S.C. §§ 102(a), 408(a), 410, 411.

Although the first design was not registered, the registration of the **Bridgeford** design sufficed for suit on the kit-and-kaboodle. See **Xoom v. Imageline, Inc.**, 323 F.3d 279, 283-84 (4th Cir. 2003); 2 Melville B. Nimmer & David Nimmer, **Nimmer on Copyright** § 7.16[B][2][c], at 7-173 (perm. ed., rev. vol. 2006).

But it was harmless error!

The judge told the jury **Phelps** was entitled to actual damages and to all profits. See 17 U.S.C. § 504. What he actually said was:

“Actual damages for infringement are measured according to market value, which means what a willing buyer would have been reasonably required to pay a willing seller for the copyright holder’s work.”

Which was the \$20-thou that **Bridgeford** paid.

Had the jury actually been paying attention to what the judge said about derivative works, they would have merely given **Phelps** the value of some altered windows.

On the profit issue, he said: “An infringer’s profits consist of the amount of the infringer’s gross revenues from the infringing activity less the expenses of producing the infringing work.”

The burden was on **Galloway** on the profit issue, and the jury was apparently satisfied with his data that showed a loss.

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Now How About That Injunction?

Phelps wanted to (1) prohibit the completion of the house, and (??) (2) prohibit its sale or lease. They argued that being made whole was not enough. Under a threat of continuing infringement an injunction was required. *Walt Disney Co. v. Powell*, 283 U.S. App. D.C. 111, 897 F.2d 565, 567 (D.C. Cir. 1990).

The Fourth Circuit said there was nothing automatic about injunction; it was entirely discretionary. See *eBay Inc. v. MercExchange, LLC*, 126 S. Ct. 1837, 1839 (2006).

Ceasing construction was moot as the house was virtually completed.

Phelps argued that they have the exclusive right to sell or lease their copyrighted work. See 17 U.S.C. § 106(3). And **Galloway** had to be shut out of this possibility for the 95 year life of the copyright.

The Fourth Circuit found an exception in the “**first sale doctrine**” 17 U.S.C. § 109(a). This permits a purchaser of a particular copy (the **Galloway** house) to sell or otherwise dispose of it. **Galloway** has paid his \$20-thou and can now sell the house.

Phelps countered that the first sale had to be a lawful one and **Galloway**’s skullduggery tainted the whole transaction and deprived him of his rights.

The Fourth Circuit said that might be true if the house sale was going down before the \$20-thou judgment. See, *Palmetto Builders & Designers, Inc. v. Unireal, Inc.*, 342 F. Supp. 2d 468,473 (D.S.C. 2004). But now after the pay-off, the house becomes a lawfully-made copy. The analogy was to a converter who got sued and paid the full value of the personal property that he absconded with. He now has title.

For you lay-folk, conversion is a blanket civil tort for any making off with someone else’s personal property, or chattel as it was once called in olde Anglo Saxon. On the criminal side this might be larceny, burglary, embezzlement, armed robbery or whatever. Which sounds like you could covet your neighbor’s ox or ass, but if he didn’t want to sell, you’d take it at gunpoint and then pay him the value. In fact, you face the criminal law as well and will be looking at jail time. So don’t try that in your own neighborhood.

In the case of patents and copyright, the first sale doctrine does not merely include voluntary sales, but might be a compulsory transfer such as a judicial sale or court-compelled assignment. The only question is whether the patent or copyright holder has gotten his just reward. *Platt & Munk Co. v. Republic Graphics, Inc.*, 315 F.2d 847,854 (2d Cir. 1963).

Phelps said a pirate taking your stuff and then paying you the value after you sue is equivalent to a compulsory license, which is largely a no-no. See *Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417, 446 n.28, 104 S. Ct. 774 (1984).

The Fourth Circuit disagreed, saying

copyright piracy was not an enforced license because the potential damages paid by the pirate were so much broader than just paying the standard license fee. In addition to the actual damages and profit disgorgement, the court might order the destruction of the infringing article. See 17 U.S.C. § 503(b). And in the ordinary theft type situation, this is typically done. See, e.g., *Loud Records, LLC v. Lambright*, Civ. No. 1:05-0171, 2006 U.S. Dist. LEXIS 38016 (S.D. W.Va., March 30, 2006).

As to houses, it’s true they contain the architect’s expression, but their character is predominantly functional. Before the Berne Convention, there was no protection for constructed architectural works at all. See 1 Nimmer & Nimmer, *supra*, § 2.08[D][2][b], at 2-126. This was changed by the Architectural Works Copyright Protection Act, but Congress has been pretty clear about not having automat-

ic injunctions on pirated building designs.

The court talks about “encumbering” all kinds of property along with the design such as swimming pool, building materials, fence, etc. What they really mean is you’d be destroying a whole bunch of value when the copyright owner had already been paid off. See *Bucklew v Hawkins, Ash, Baptie & Co.*, 329 F.3d 923, 931 (7th Cir. 2003).

What **Phelps** has frosted is not just the usual moral indignation over someone taking your design, but the fact that they got no disgorgement of profits. Otherwise, **Galloway** doesn’t own their design and can’t copy it in another house.

Unless, I guess, he rushed and built it in its entirety before they caught him again. Perhaps he could put up a whole sub-division of identical Phelps’ designed French-country houses. 🐼

Questions & Answers — Copyright Column

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QUESTION: *How are oral history recordings and transcripts affected by copyright? Once the interviewee is deceased, does the library that holds the recordings and transcripts have any restrictions?*

ANSWER: Oral histories present interesting copyright issues for libraries. Older histories, such as those recorded as WPA projects during the Depression, may have little documentation concerning releases, etc. Today, most interviewers require the interviewee (person being interviewed) to sign a release. The release states what will be done with recording, the transcript, etc. Assuming that there is no release oral histories clearly belong to the interviewee, although the interviewer may hold copyright



in the question he or she poses. The most important material, however, is the text or words spoken by the interviewee, and the interviewee owns the copyright in his or her words.

Through a release, the interviewee may give the library all rights to use, publish and distribute via the Web an oral history. Death of the interviewee changes only who owns the copyright. It passes to the heirs of the deceased interviewee; therefore, the library still may not do as it pleases with the recording and transcript unless there was a release that permits it to publish, distribute, etc.

QUESTION: *A library has a cost-recovery outreach program where it provides library services for small hospitals that do not have a library or only have a core collection, for attorneys and for individual health care professionals. The program provides reference service including searches of the literature, training on locating medical information, and supplies copies of books and articles, either from its collection or via interlibrary loan from another library. When using interlibrary loan, does it matter if the patron is an unaffiliated patron? Should the lending library be notified of the status of the user? Is this activity “systematic” distribution under section 108(g)(1)?*

ANSWER: The unaffiliated status of the user is not particularly relevant in the interlibrary loan equation. The issue is whether the borrowing library counts the ILL request in its suggestion of five and pays royalties when it exceeds the CONTU guidelines. If the user’s request will take the library over the suggestion of five, then royalties should be included in the cost recovery calculation. The legislative history that accompanied the Copyright Act indicated that while the system of interlibrary loan may be systematic, the use of ILL alone does not violate section 108(g)(1).

QUESTION: *Is the library liable when a user infringes copyright by downloading from an electronic database an entire online textbook?*

ANSWER: Generally no. License agreements typically detail the rights and

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